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Remarks by William Murray

Vice Chairman of the Board

Philip Morris Companies Inc.

at the

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Thank you. I am delighted with this opportunity to meet you and to talk with you about the tobacco industry. Philip Morris was built on tobacco and I assure you it will remain our core business.

Tobacco makes an extraordinary contribution to our overall business. At the same time, we cannot ignore the fact that tobacco is a controversial product, and that in choosing to manufacture and market cigarettes, we face many challenges. Given these two factors -- tobacco's importance to us and the controversial issues surrounding it -- I thought you might find it useful if I shared with you my outlook on the tobacco industry in the years ahead in light of the problems we face, and the plans we have to deal with them.

The problems are real, they are serious and I do not intend to gloss over them. But it is my firm belief that every problem we face is manageable. It is also well to remember that we are not the only industry faced with serious problems and strident critics. I will return to this point a little later.

Also, as I look at each problem, I want you to keep the following facts in mind. In 1988, our tobacco operations -- domestic and international -- accounted for 82 percent of our operating income. In 1989 after the Kraft acquisition, tobacco is providing 68 percent of our operating income. At the end of the current five year plan in 1993, tobacco will still contribute 66 percent of our operating income.

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What, then, are the problems that can significantly impact this most valuable component of our business. I will begin with environmental tobacco smoke or ETS, as it is probably the single most important challenge we currently face. ETS is the driving force behind smoking restrictions in the workplace, on airlines and other forms of public transportation, and in virtually all areas offering public access.

If present trends continue, smokers will have fewer and fewer opportunities to enjoy a cigarette. This will have a very direct and major impact on consumption -- an impact which will be as bad as, or worse than, excise tax increases.

To date, our principal defense has been the position developed by indoor air quality scientist Gray Robinson -- that there are many other things to blame for poor indoor air quality, and tobacco smoke is only a small part of the problem.

We must find stronger arguments to support our position on ETS. We have made this a principal thrust of PM USA's corporate affairs activities. We have formed a task force headed by Nelson Beane, Senior Vice President of Business Development, to develop cogent, effective arguments on the issue. Some will come out of the scientific literature, because many studies do not support the claim that ETS is harmful to the non-smoker.

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We have hired a scientific writer who will put supporting material into layman's language, and we have hired a public affairs person who will place these messages with the media for dissemination to the general public.

The Council for Indoor Air Research is now up and operating. Funded by the tobacco industry, the Council will commission independent research on ETS. We expect that in the long term, new, unbiased studies will provide an effective rebuttal to the earlier studies conducted by avowed anti-smoking researchers.

Also in the long term, the Tobacco Institute is identifying reputable medical researchers who do not believe ETS is harmful to the non-smoker and who will speak out on this issue. A similar program is already underway internationally.

I am convinced that with these and similar programs we can defuse ETS as a central issue, but this is going to take time, energy and a significant commitment of resources.

A second issue of major importance is excise taxes. Excise tax increases and the resulting increase in consumer prices produce a direct and immediate reduction of total market size. Of particular concern are ad valorem taxing systems as contrasted with specific or fixed systems. Ad valorem systems disadvantage Philip Morris as we generally sell our tobacco products in the higher price categories.

Our objective is to minimize excise tax increases both at the national and state level and also, very importantly,

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to make sure that excise taxing formulae or systems do not disadvantage our products.

Excise taxes will continue to be an issue of constant and priority concern to us both in our international markets and in here in America. In the U.S., managing the problem depends on the level of government involved.

At the federal level, we have been reasonably successful in heading off federal excise tax increases and I think we can continue to do this. We have applied a lot of resources at the federal level. We have an administration that is fundamentally opposed to tax increases. And we have a Democratic House and Senate where a large part of the membership accepts the regressivity theory and will hesitate to raise a tax that forces those who can afford it least to pay the most. These facts make me reasonably confident that we will be able either to avoid or contain federal excise taxes for the foreseeable future.

The situation at the state level is quite different and this is what worries me. First, we do not have the fire power in each of the 50 states that we have in Washington. Our efforts at the state level are much more fragmented. Second, in contrast with the White House, many state Governors are in favor of increased taxation. Lastly, a number of states have acute budget deficit problems.

For PM USA to battle state tax increases effectively, we must bring more resources to bear on the problem -- more

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contract lobbyists and tighter coordination between the PM state network and the Tobacco Institute's network.

Additionally, we must try to find ways of harnessing the total resources of PM Companies Inc. to deal with the problem. We have plants in virtually every state in the Union. We must use our overall corporate influence to combat excise tax increases state by state, legislature by legislature.

Internationally, my biggest concern on excise taxes relates to an issue that has been discussed at this conference -- the formation of the unified internal market of the European Economic Community in 1992. There is a clear risk that a uniform system of taxing cigarettes will be adopted which will incorporate the highest overall tax rates existing today in the Community. There is also a risk that an ad valorem taxing system will be used and that our higher priced products will be disadvantaged.

We must fight to make sure this does not happen. It is my single biggest concern about the formation of the common internal market and we are applying a lot of management time and effort to the issue.

A third major issue is, of course, product liability. It is a central issue of this conference and so I am not going to say much about it except to tell you that the management of this company is committed to applying whatever resources are necessary to the issue of product liability. We will continue to defend our position vigorously. I am

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confident that, with your help, the product liability issue will be a manageable one.

A fourth issue we face is discrimination. Discrimination against smokers is becoming commonplace, particularly in the United States. You have only to look in the "Help Wanted" ads of The New York Times to see that many ads contain the phrase, "Smokers need not apply" or some similar, discriminatory message.

When a person's actual livelihood is endangered -- his ability to support his family -- as a result of using a legal product, we cannot stand idly by. And we do not intend to.

The practice of discrimination is scorned by the majority of Americans. Our objective is to capitalize on the deep and abiding value Americans place on equal treatment and to have bills passed wherever we can that will protect those who choose to smoke from discrimination based on that choice. This will be a major project in the years ahead. So far, anti-discrimination bills protecting smokers have been passed in Virginia, recommended for study in Arkansas and Mississippi and introduced in state legislatures in Delaware, Illinois, Maryland, Nevada and Oregon. I am confident that this is an issue on which we will have a good measure of success in the years ahead.

A fifth issue which prompts wild allegations from the Surgeon General and others is that of the so called "social costs" of smoking, costs which are claimed to be borne by

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the health care system, non-smokers and society generally. The figures have no basis in reality; they are simply plucked from the air or generated from erroneous theory and methodology.

Extravagant and flawed as they are, social cost arguments are a real issue for us because they are used to justify increased taxation. If the antis succeed in branding smoking as a cost to society, the next step will be to require smokers to pay all or part of that cost. It also leads to increased insurance premiums and other treatment which is unfair and discriminatory.

What are doing about it? We have taken and will continue to take a proactive stance in issues advertising and other communications programs which identify smokers and the tobacco industry as an economic asset to society.

We are also disseminating information that effectively reduces the social cost theory to its absurd underpinnings. Because the social cost argument can be applied to virtually every activity in a society -- sports, watching television, eating in restaurants, having children, maintaining a system of representative government, and so on -- it becomes a meaningless argument.

In conjunction with the Tobacco Institute, we are developing relationships with economists who share our view that the social cost argument is patently absurd and who are prepared to argue the case with our opponents. Because the social cost argument is advanced primarily by doctors and

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others in the health care field who usually do not have expert knowledge of economics, they are quite vulnerable in debates with professional economists.

We are also participating in the Social Cost Council, set up by the U.S. Chamber of Commerce and composed of major industries which are subject to, and oppose, taxes and regulations based on social cost arguments.

Finally, even if one accepts the premises of the social cost theory, which we do not, and all the factors are taken into account, analyses by the Rand Corporation and the National Bureau of Economic Research reject the social cost argument.

As we succeed in having the myth of social costs exposed for what it is, and as we help the public and decision makers understand the false reasoning involved, I believe that we can manage the social cost issue effectively.

Sixth, we have to confront marketing restrictions. Many countries impose restrictions on our ability to freely market our products and to compete on an equal basis. We will continue to vigorously oppose all of these kinds of restrictions.

Again, to use the United States as an example, several bills designed to restrict our marketing ability either have been or will be submitted to Congress. These bills include bans or severe restrictions on advertising; the withdrawal or amortization of the tax deduction for advertising

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expenditures; bans on vending machine sales and sampling; and bans on event sponsorship and other forms of promotional activities. One bill, introduced by Congressman Levine of California, would even put the United States in the curious position of exporting censorship.

Although we have not won every battle, we have been reasonably successful both here and abroad in dealing with these kinds of proposals. I am quite confident that we will continue to do so in the future and I do not see a groundswell movement toward a highly restrictive marketing environment either here in the U.S. or overseas.

Seventh, increased government regulation of our industry is emerging as a major issue. Additive laws or regulations could be adopted in the European Economic Community in 1992. In the United States, Congressman Whittaker of California has a bill before Congress which would place the cigarette industry under the control of the Food and Drug Administration. This would put very severe controls on product content, particularly in the area of additives used in our products.

We will vigorously oppose these initiatives. The thrust of our activities will be to retain the status quo or to have rules adopted which are sensible and with which we can comply, such as those existing in the U.K. or Germany.

Finally, there is the issue of social acceptability. Smokers are becoming social pariahs. The choice to smoke, which was once considered a social grace and a mark of adult

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sophistication, is more and more becoming a socially unacceptable practice.

This change is a major concern to us and the industry as a whole, and PM will have to be more effective in dealing with this trend than we have in past years.

We intend to approach the social acceptability issue on several fronts. To a large extent it is linked to the ETS issue that I talked about earlier -- the theory that my smoking damages your health. If we can be more successful in dealing with the ETS issue, it will help us on social acceptability.

Another point where we can attack is the downright zealotry and extremism of our opponents. We need to develop programs that expose the anti-smoking activists for what they are -- shrill and extreme. If we are successful in revealing to the public the zealots, the blind crusaders for a cause, this will mitigate pressures on social acceptability.

In short, we have got to find ways to put the choice to smoke into the more relaxed environment that surrounds other controversial issues or products. This won't be easy, and it is long term assignment, but I am confident that we can find ways to alleviate the social pressures currently being put on smokers.

Before I conclude I would like to take a second to put the problems of our industry in perspective. The environmental movement begun in the 60s in the U.S. brought

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great pressures to bear on the oil industry. This "fossil fuel" industry, perceived as faceless, multinational, monolithic and conspiratorial, produced a product claimed by many to be be the worst environmental pollutant. Its exploration, drilling, extraction, pumping and pipelines were equated with the systematic decimation of the environment.

The OPEC oil embargo of the 70s, lines at gas stations, increased prices and all the rest or the fallout focused the controversy and created an outcry from the public and proposals from extremists to dismantle the industry in favor of alternative fuel sources -- wind, solar, geothermal, wave and tidal powered generators and, of course, nuclear.

But let me ask you something. It's 1989 and who came to this conference in an electric car? How many of you heat your homes with coal? Light your living rooms with electricity generated from a volcanic vent?

Even as I speak, with Exxon's ten million gallon black mark rolling in on the port of Valdez, Alaska, and with nuclear energy cartoons tieing Uncle Sam's fuel needs to the fickle finger of Ayatollah Khomeini, the oil industry is alive and well.

It is no coincidence that aggressive, proactive, effective issues-targeted programs were applied -- indeed <u>invented</u> -- by the oil industry.

We are not the only industry with problems. At some time or other, every industry -- everything from oil and

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nuclear, to chemicals and cars, to baby food and apples -- has problems. Yes, ours are often on a grander scale, and our opponents seem particularly driven by the demons of overzealous moral righteousness, but we have the brightest and most committed people to address our problems, confront our critics and fight for our rights and those of our customers.

And that, in conclusion, brings me to you. Many of the problems I have touched on tonight involve your professional skills. My challenge to you is simple. We need you to bring your most creative, your most thoughtful and intelligent, your most professional abilities to bear on the problems I have set forth. We need your best.

To give it, you are bound to move into areas which are new to you. Traditionally, attorneys play an advisory role in business, one that is often relatively narrow and circumscribed. We ask much more of you. We need ideas as much as we need advice.

Our post-verdict rebuttal of the Cipollone plantiff law team's selective presentation of research on smoking and health is a case in point. Our lawyers conceived of and wrote that document, which showed point by point how information was misrepresented by the plantiff lawyers and exploited in anti-smoking public relations press releases. Our law team's response, geared to the lay reader and distributed to the press, was enormously helpful in our public relations effort and in the education of our own

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employees on the issues, the techniques used against us and the truth of the matter.

As trained professionals, you have a unique ability to examine the arguments of our opponents and, in many cases, explode them. Any time you see the opportunity to share this kind of thinking with those who articulate our positions publicly, please do so.

As creative thinkers, I am sure you also have ideas that are not necessarily legal concerns, but bear on the operations, marketing, sales, information systems, entrepreneurial opportunities and public affairs strategies of our tobacco operations -- ideas that may well be enormously helpful to management in other departments and even other PM companies. We speak a lot about synergies at Philip Morris. When we do, we mean the sharing of this kind of information.

What is comes down to is this: as Philip Morris employees, thinkers and advisors, you are our most valuable resource. And we need that resource very much. So, again, I challenge you to give us your best. With it, I can assure you that the problems we face are managable and that we will prevail.

Thank you.

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